

A Leader in Accounting Education

Accountancy@UJ**TAXATION PLANNING 2B [TXP2B01]****FINAL ASSESSMENT OPPORTUNITY****1 November 2014**

Examiner: **Ms M Lephoto**
 Moderator: **Ms M Wassermann**

Time: **2.5 hours**
 Marks: **125 marks**

INSTRUCTIONS TO CANDIDATES:

This paper consists of 8 pages and an appendix. Ensure that no pages are missing.

Show all calculations, workings and reasoning clearly.
--

Silent, non-programmable calculators may be used.

Do NOT use any tippex .

Refer to the mark allocation as a guide as to the amount of time to spend on each question.

You are reminded that answers may NOT be written in pencil.
--

Round off answers to the nearest Rand.

Summary of Questions and Time

Question	Marks	Time
1	45	54 Minutes
2	25	30 Minutes
3	15	18 Minutes
4	30	36 Minutes
5	10	12 Minutes
Total	125	150 Minutes

QUESTION 1

(45 Marks)

Kermit Fogg (hereafter Kermit) has always loved tea. Upon retirement, Kermit decided to open up a “tea spot”. He registered a close corporation and named it Kermit Teas CC (hereafter KTCC). KTCC is voluntarily registered for VAT on the invoice basis and has a December year end.

Kermit believes in the healing properties of tea and its overall health benefits. He believes that if the people of Johannesburg could be introduced to different types of tea, their consumption of sugar laden soft drinks would decrease and so would the incidence of diabetes.

Kermit purchased a building in The Maboneng Precinct. He acquired the building from Propertuity, a property development company that is spearheading the urban regeneration of this part of the Johannesburg CBD; Propertuity is a VAT vendor. The Maboneng Precinct is an urban development zone.

This building was old and dilapidated until it was refurbished by Propertuity. Kermit bought it for R684 000 on 1 January 2012.

KTCC imports teas from all over the world and sells them to the public.

All amounts include VAT unless otherwise stated.

The following information relates to the 2014 year of assessment:

1. Local tea sales for the year amounted to R570 000.
2. Purchases of tea for the year amounted to R114 000.
3. The value of the teas on hand on 1 January 2014 was R 34 000 (excluding VAT). As at 31 December 2014, stock on hand was valued at R 22 000 (excluding VAT).
4. Kermit sold Chinese slimming tea to his girlfriend, Miss Piggy, for R500 (excluding VAT) when the market value was R 600 (excluding VAT). This sale was not included in the sales figure in point 1 above.
5. Kermit employs a cashier, a driver and a cleaner.
 - Salaries and wages paid R102 000
6. Kermit’s acquaintance, Mr. Muppet, approached him with the idea of brewing a tea that could cure arthritis. Mr. Muppet had travelled extensively in the East and had amassed a vast knowledge in the field of herbal remedies.

Kermit applied to the Minister of Science and Technology for approval of the research and development which was granted in December 2012.

Question 1 continued.....

In order to enable Mr. Muppet to develop his idea, Kermit acquired an adjoining building for R228 000 on 1 January 2013 and set to work converting it into a laboratory; conversion cost was R 45 600. The laboratory was brought into use on 5 June 2013.

Mr. Muppet requested lab assistants to be employed who were paid R50 000 for the 2014 year of assessment. On 10 May 2014, KTCC received a grant of R25 000 from the Department of Health to fund the research and development regarding the AthroTea™.

Mr. Muppet completed his work and on 1 February 2014. A patent was registered on the formula for the tea; registration cost R 2 565.

Kermit came up with the name ArthroTea™ and registered a trade mark over it in February 2014 at a cost of R 5 700.

The teabag had a unique pyramid shape that was designed by Mr. Muppet; KTCC purchased the design from Mr. Muppet for R 9 200 on 1 March 2014.

7. In order to manufacture the ArthroTea™ for sale, KTCC entered into a lease agreement for a piece of vacant land two streets from the current premises.

The lease commenced on 1 July 2013 and the details are as follows:

- Lease term equals 30 years.
- A lease premium of R180 000 (excluding VAT) was paid on 1 July 2013.
- The monthly rental expense is R45 000 (excluding VAT).
- A factory building has to be erected at a cost of R800 000 (excluding VAT).

Building commenced on 1 July 2013 and was completed on 30 June 2014 at a cost of R 950 000 (excluding VAT). The factory became operational on 1 July 2014.

8. New manufacturing machinery was purchased and brought into use on 1 July 2014 to mass produce the AthroTea™; cost price R399 000.
9. There was great international interest in the AthroTea™. Export sales made amounted to R800 000.
10. The driver wrote off the delivery vehicle on 30 November 2014 when he crashed into a tree trying to avoid a dog that was crossing the street. The insurance paid out an amount of R684 000.

The delivery vehicle had been purchased on 1 February 2012 at a cost of R 570 000.

The write off period for delivery vehicles per Binding General Ruling 7 is 4 years.

11. Kermit Teas CC had an assessed loss of R5 000 in the previous year of assessment.

YOU ARE REQUIRED TO:

Calculate the **normal tax liability** of Kermit Teas CC for the year of assessment ended **31 December 2014**. Show all calculations. If any amount should **not** be included in your calculation, state the reason why. (45)

QUESTION 2

(25 Marks)

Rhodes (Pty) Ltd is a resident company with a 31 December year end. The company **is NOT a small business corporation**. The company is registered for VAT.

All amounts include VAT where applicable, unless stated otherwise.

1. On 1 August 2014, Rhodes (Pty) Ltd acquired a new manufacturing asset to use in the business at a cost of R342 000. On 31 December, 2014 they incurred moving costs of R28 500 on this asset.
2. On 1 June 2001, Rhodes (Pty) Ltd acquired a second-hand manufacturing asset at a cost of R684 000. In November 2014, Rhodes (Pty) Ltd sold the asset for R798 000.

The market value on 1 October 2001 was R540 000.

YOU ARE REQUIRED TO:

Calculate the **income tax consequences** of the two transactions above for Rhodes (Pty) Ltd's 2014 year of assessment.

(25)

QUESTION 3

(15 Marks)

Moitheri “Terry” Pheto (hereafter Terry), born 11 May 1981, is a South African actress best known for her leading role as Miriam in the 2005 Oscar-winning feature film *Tsotsi*. Since then she has landed roles in several international productions including the role of Dr. Malaika Maponya in *The Bold and the Beautiful*.

Terry is a resident of South Africa. In the 2014 year of assessment, she received the following amounts:

1. Dividends:
 - a. From South African companies R20 000
 - b. From foreign companies R10 000(She owns 1% of the equity interest in the foreign company and paid the equivalent of R1 500 in foreign taxes.)
2. Interest
 - a. From a South African bank R50 000
 - b. From an American bank R30 000(She paid the equivalent of R2 000 in foreign taxes.)
3. Terry recently signed an endorsement deal with L’Oreal Paris as the face of its new range in South Africa. Consequently, Terry has been featured in a number of television advertisements and done magazine photo shoots in South Africa.

In terms of the double tax agreement (DTA) between South Africa and France, the source of service fees is the country in which the services are rendered. However, L’Oreal Paris withheld 5% of her fee and paid it over to the French tax authorities. The tax is not recoverable.

In the 2014 year of assessment, Terry received the equivalent of R500 000 as an endorsement fee.

4. Rental income R100 000
Terry owns an apartment in Los Angeles which in she stayed during her time on *The Bold and the Beautiful*. After her role ended, she decided to keep the apartment and rent it out. She is never without tenants owing to the steady stream of South Africans who keep going to America in the hope of making it in Hollywood. Foreign taxes paid on the rental income amount to the equivalent of R10 000

Assume that Terry received no other income and incurred no deductible expenditure.

YOU ARE REQUIRED TO:

Calculate Terry Pheto's **normal tax liability** for the year of assessment ended **28 February 2014**. Terry has **elected s6quat (1C)**. **(15)**

QUESTION 4

(30 Marks)

John Msimanga (hereafter John) is a businessman from the sleepy town of Tweeling in the Free State. He trades as a sole proprietor. He owns a supermarket, rents out a house to tenants and owns a few cows.

10% of his total turnover comes from renting out a house to tenants.

John is a category B VAT vendor and he accounts for VAT on the invoice basis.

John's wife, Emily Msimanga (hereafter Emily), whose highest qualification is a matric certificate, is the bookkeeper and is responsible for all accounting records. She is also required to complete the two-monthly VAT returns.

Emily has gone behind her husband's back and requested your help processing the following transactions through the accounting records. She has **not recorded** any entries in the accounting records for the following transactions as she is unsure of the VAT implications. All transactions relate to the **VAT period ending 30 April 2014**.

Transaction 1:

John incurred the following expenses per month:

Salaries	2 710
Purchases of trading stock	1 710

Transaction 2:

The population of Tweeling is very small and the town has high levels of unemployment. Consequently, John's business has been experiencing cash flow problems. In order to stimulate cash flow, John took out a loan from ABSENT BANK on 1 January 2014. Monthly interest on the loan amounts to R240.

John has only one business bank account which he opened at ABSENT BANK. The bank charges John monthly bank charges of R399.

Transaction 3:

John has ambitions of growing his business. He knows that the best way to do this is to network. He decided to take up golf as a hobby. On 1 April 2014, John joined the Reitz Country Club. He paid membership fees of R314 per month.

Transaction 4:

John earned the following income for the two month VAT period:

Nature of Income	Amount (R)
Supermarket cash sales	22 800
Supermarket credit sales	12 540
Sale of Milk from the cows he keeps	2 280

Half of the supermarket credit sales were written off as a bad debt at the end of April 2014.

Transaction 5:

John's parents died about ten years ago having both lived full lives. As the oldest male amongst his siblings, John inherited his parents' one bedroom house. Being the businessman that he is, John decided to let the house to tenants from 1 January 2014 at a rate of R625 per month. The water and electricity bill for the house amounts to R300 per month, which is paid by John.

Transaction 6:

In the recent floods that hit the Eastern Free State, John's supermarket was heavily flooded. Most of John's stock was damaged in the flood and was rendered unusable. Platteland Insurance company paid John for damages suffered amounting to R36 000.

Transaction 7:

Emily advised John to purchase a computer so as to enable her to submit the VAT returns via e-filing. John purchased a second hand computer from a local teacher who had bought himself a laptop. John paid R 2 600 which is below the market value of R 3 000. The computer will be used in all of John's business ventures.

YOU ARE REQUIRED TO:

Provide Emily with the **journal entries** for the above transactions. Give **reasons for the VAT treatment as journal narrations** so that Emily understands. **All amounts include VAT unless stated otherwise in the question.**

QUESTION 5**(10 Marks)**

1. What is the difference between **tax avoidance** and **tax evasion**? (2)
 2. Explain briefly what **s 103(2)** of the Income Tax Act is about. (2)
 3. Name the three requirements that must be met for **s 103(2)** to apply. (3)
 4. Define an **intragroup transaction** in terms of **s45** of the Income Tax Act. (3)
-

Appendix A : Rates of tax

SLIDING SCALE APPLICABLE TO A SMALL BUSINESS CORPORATION

Years of assessment ending during the 12 month period ending on 31 March 2014

0 – R67 111	0%
R67 111– R365 000	7% on amount exceeding R67 111
R365 000-R550 000	R20 852 + 21% on amount exceeding R365 000
Above R550 000	R59 702 + 28% on amount exceeding R550 000

NORMAL TAX RATES PERSONS OTHER THAN COMPANIES AND TRUSTS

Year of assessment ending 28 February 2014

Taxable Income		Rates of taxes	
Exceeds	Does not exceed		
R	R	R	R
0	165 600	0 + 18% of each R1	
165 601	258 750	29 808 + 25% of the amount above	165 600
258 751	358 110	53 096 + 30% of the amount above	258 750
358 111	500 940	82 904 + 35% of the amount above	358 110
500 941	638 600	132 894 + 38% of the amount above	500 940
638 601	+	185 205 + 40% of the amount above	638 600

